IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

No. 615

FERNAND C. A. ADDA,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT.

HUGH SATTERLEE,
MITCHELL B. CARROLL,
ROLLIN BROWNE,
Attorneys for Petitioner.

Pandick Press, Inc., 22 Thames St., New York 6, N. Y., U. S. A.

INDEX.

CITATIONS.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

No. .....

FERNAND C. A. ADDA,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The petitioner prays that a writ of certiorari issue to review the judgment (R. 37) of the United States Court of Appeals for the Fourth Circuit, affirming the decision of the Tax Court of the United States (R. 10).

OPINIONS BELOW

The opinion of the Tax Court is reported in 10 T. C. 1291. The *per curiam* opinion of the Court of Appeals is not yet reported, but is printed in the transcript (R. 36).

JURISDICTION

Jurisdiction to issue the writ prayed for is vested in this Court by Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925. The judgment

of the Court of Appeals was entered on December 3, 1948 (R. 37).

QUESTIONS PRESENTED

1. Is the specific provision of Section 211(b) of the Internal Revenue Code, that effecting transactions in securities and commodities by a nonresident alien through resident brokers does not constitute engaging in business here, rendered inapplicable merely because the transactions were effected on orders given to the resident brokers by a resident agent of the nonresident alien?

2. Aside from the specific provision of Section 211(b) referred to in the previous question, does the buying and selling of commodities futures by an individual for his own account for investment or speculation, as distinguished from buying and selling property as a broker or dealer for customers, constitute engaging in trade or business within the meaning of Section 211 of the Internal Revenue Code?

STATUTE INVOLVED

Internal Revenue Code, as in force in 1941:

SEC. 211. TAX ON NONRESIDENT ALIEN INDIVIDUALS.

(a) No United States Business or Office.—

(1) General Rule.—

(A) Imposition of Tax.—There shall be levied, collected, and paid for each taxable year, in lieu of the tax imposed by sections 11 and 12, upon the amount received, by every nonresident alien individual not engaged in trade or business within the United States and not having an office or place of business therein, from sources within the United

States as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, a tax of 27½ per centum of such amount, except that such rate shall be reduced, in the case of a resident of any country in North, Central or South America, or in the West Indies, or of Newfoundland, to such rate (not less than 5 per centum) as may be provided by treaty with such country. . . .

(b) United States Business or Office.—A nonresident alien individual engaged in trade or business in the United States or having an office or place of business therein shall be taxable without regard to the provisions of subsection (a). As used in this section, section 119, section 143, section 144, and section 231, the phrase "engaged in trade or business within the United States" includes the performance of personal services within the United States at any time within the taxable year, but does not include the performance of personal services for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of ninety days during the taxable year and whose compensation for such services does not exceed in the aggregate $3,000. Such phrase does not include the effecting of transactions in the United States in stocks, securities, or commodities through a resident broker, commission agent, or custodian.

SUMMARY STATEMENT OF MATTER INVOLVED

Section 211(b) of the Internal Revenue Code, first enacted in 1936, provides that the effecting of commodities and securities transactions in this country by a nonresident alien through resident brokers does not constitute engaging

in trade or business here. Under Section 211(a) of the Code gains realized on such transactions by a nonresident alien not otherwise engaged in trade or business in this country are not subject to income tax.

Petitioner, a nonresident alien never in the United States, admittedly not otherwise doing business in this country or having an office or place of business here, bought and sold commodities through resident brokers for a number of years, transmitting his orders to his brokers from abroad through regular channels of communication. During the war, because of the temporary disruption of communications, although petitioner was able to some extent to send orders directly to his New York brokers, he also authorized his brother, who was in the United States, to give orders to petitioner's brokers for petitioner's account, using his discretion within the scope of certain general instructions which petitioner gave him as to the trading policies to be followed.

The Tax Court, disregarding the express provision of Section 211(b), held that the transactions in 1941 thus effected for petitioner's account on the orders given to his brokers by his brother constituted engaging in business in this country, apparently on the ground that such transactions were "effected" through petitioner's brother and not through resident brokers. The Court of Appeals affirmed on the opinion of the Tax Court, but from various remarks made from the bench during the argument it appears likely that the Court of Appeals was influenced by a feeling that the method of taxation provided in Section 211(a) was not intended to apply to transactions in commodities and securities which were so regular and extensive that they might conceivably constitute carrying on business within the concept of the income tax law in the absence of the express exception in Section 211(b).

Whatever may have been the rationale of the decision below, it fails to give to Section 211 the ordinary scope of its clear and unambiguous language and, in thus attempting to restrict its scope, throws into confusion the entire scheme for taxation of nonresident aliens. It also raises questions as to the interpretation of tax treaties between the United States and various foreign countries, which follow a similar pattern.

SPECIFICATION OF ERRORS

The Court of Appeals erred:

1. In holding that the effecting of commodities transactions by petitioner through resident brokers, on orders given to the brokers for petitioner's account by petitioner's brother while in this country, constituted carrying on trade or business here.

2. In holding that the buying and selling of commodities futures by petitioner for his own account for investment or speculation, and not as a broker or dealer for customers, constituted carrying on trade or business within the meaning of Section 211 of the Internal Revenue Code.

3. In holding that the petitioner is subject to income tax on the gain resulting from such transactions.

4. In affirming the decision of the Tax Court.

REASONS FOR GRANTING WRIT

1. The Court of Appeals has decided a novel and important question of federal tax law which has not been, but should be, settled by this Court.

In the Revenue Act of 1936 Congress first adopted the plan of taxing nonresident aliens and foreign corporations not engaged in trade or business within the United States (or having an office or place of business here) at a fixed rate on their ordinary periodical income from sources within this country, excluding capital gains, but without the benefit of deductions and credits, and taxing nonresident aliens and foreign corporations engaged in business within the United States (or having an office or place of business here) in the same manner as residents and domestic corporations, to the extent of their net income from sources within this country. (R. A. 1936, now I. R. C., Secs. 111, 131) A succinct explanation of the new system was given by the Committee on Finance of the Senate as follows (Report No. 2156, 74th Cong., 2d Sess., p. 21):

> ". . . Such a nonresident alien [not engaged in trade or business here] will not be subject to the tax on capital gains, including so-called gains from hedging transactions, as at present, it having been found administratively impossible effectually to collect this latter tax. It is believed this exemption from tax will result in considerable additional revenue from the transfer taxes and from the income tax in the case of persons carrying on the brokerage business. . . .
>
> In the case of a nonresident alien engaged in trade or business in the United States or having an office or place of business therein, the same tax is levied upon his net income from sources within the United States as is levied upon the American citizen or resident under the House bill. Your committee concurs in this plan but recommends amendments to section 211(b) of the House bill which are intended to clarify the meaning of the phrase 'engaged in trade or business in the United States'."

The meaning of the last sentence of Section 211(b), which was added in the Senate expressly to clarify the meaning of the phrase "engaged in trade or business in the United States", has been brought in question by the decision below. The phrase "engaged in trade or business within the United States" "does not include the effecting of transactions in the United States in stocks, securities, or commodities through a resident broker, commission agent, or custodian". The statement is unqualified. Yet the Court of Appeals would seem to interpolate the requirements that the nonresident alien may not act by an agent, especially one to whom any discretion is granted, and that the transactions may not be numerous. In order to prevent giving effect to the established principle of the law of agency that the acts of an authorized agent, with or without discretion, are the acts of the principal,—*qui facit per alium facit per se* (C. J. S., Agency, sec. 1, p. 1023),—it is suggested that an express denial in the statute of the right to act by an agent would be necessary. Similarly, a limitation of the provision to casual or sporadic transactions would make it mere surplusage, since such transactions never have been thought to constitute carrying on business, and would also defeat the purpose of the statute to attract trading to American markets.

It has been admitted on behalf of the Commissioner that, if a nonresident alien effected transactions in this country through an agent residing abroad, he would not be subject to tax, and yet the only transactions which could give rise to the tax, the actual sales, would occur in the United States, irrespective of the residence of the agent. The Commissioner has also conceded that a nonresident alien while in the United States may effect transactions here through resident brokers without liability to tax. (See *Constantinescu* v. *Commissioner,* 11 T. C. 36, 40). Thus, according

to decisions below, a nonresident alien individual present in the United States or who acts by a foreign agent is not subject to tax, while a nonresident alien not present in the United States who acts by an agent in this country is taxable.

The emphasis of the court below on the use of discretion in the United States may raise the further question as to whether the alien would be liable if the agent did not use any discretion in the United States but merely carried out the express instructions of the principal. It also raises the further question whether, if the nonresident authorized a broker to use discretion in placing orders for him, this would change the broker into an agent in the sense of the lower court and make the nonresident taxable.

The enactment of Section 211(b) in the Revenue Act of 1936 constituted an invitation and encouragement to nonresident aliens to buy and sell securities and commodities on the exchanges in the United States through resident brokers. It is common knowledge that many hundreds of nonresident aliens have availed themselves of such invitation to the substantial profit of United States brokers and with the benefit to the United States Treasury of taxes on such profit. The confusion as to the construction of the plain language of the statute engendered by the decisions below will, unless dispelled, inevitably cause reluctance on the part of foreign investors to trade on United States exchanges and consequent reduction in the tax benefits envisaged by Congress in enacting Section 211. This is a matter of importance to the revenue.

Section 231 of the Code, similarly to Section 211 in the case of nonresident alien individuals, divides foreign corporations for tax purposes into two classes. As these sections originally read, the maintenance of an office or place of business in the United States, equally with engaging in trade or business here, was a ground for subjecting the

nonresident alien or foreign corporation to tax like citizens and residents of the United States and domestic corporations on income from sources within the United States. By the Revenue Act of 1942 the reference to having an office or place of business in the United States was eliminated, because, as explained in the reports of the Congressional Committees (Ways and Means Committee Report No. 2333, 77th Cong., 2d Sess., p. 103; Finance Committee Report No. 1631, 77th Cong., 2d Sess., p. 135), a tendency had arisen on the part of some nonresident alien individuals and foreign corporations to attempt to establish offices or places of business within the United States in order to secure the different, and in their case more favorable, tax treatment accorded taxpayers under Section 211(b) and Section 231 (b), including the allowance of deductions and credits, although they did not engage in trade or business in the United States within the provisions of subsection (b). (See *Scottish American Investment Co.* v. *Commissioner,* 323 U. S. 119.) This situation points up the fact that subsections (a) of these sections are by no means ordinary exemption provisions, but that, to the contrary, they often increase the tax burden of nonresident alien individuals and foreign corporations.

The decision below in the present case, if sustained, would offer a much easier method to such nonresident alien individuals and foreign corporations voluntarily to avoid the tax on gross income under subsection (a) and obtain the advantage of being taxed on net income under subsection (b), contrary to the purpose of Congress in enacting the 1942 amendment. All they would need to do, instead of setting up an office or place of business in the United States, would be to appoint and act by an agent here in effecting transactions on the commodities and securities exchanges. Thus, the classification provided in subsections (a) and (b),

based on differences of substance, could be changed at will without in any way affecting the character of the transactions under general law, because in either case the transactions would, in the eye of the law, be effected by the alien on the floor of the exchange through his brokers.

2. The Court of Appeals has decided a question of substance concerning the construction and application to citizens of foreign countries of a statute of the United States closely related in application to treaty provisions, which has not been, but should be, settled by this Court. It transcends in importance a merely internal revenue provision.

The decision of the Court of Appeals raises serious questions affecting the relations of this country to residents of foreign countries, with some of which countries the United States has negotiated tax treaties containing provisions of similar purport to the statutory provision here involved. Section 211 has application only to foreigners residing outside the United States and is important only to them. Therefore, it should be interpreted according to the ordinary meaning of the English language in which it is written. "The words of a statute are to be taken in the sense in which they will be understood by that public in which they are to take effect." (*United States* v. *Isham*, 17 Wall. 496, 504.) To place upon such statute a narrow and strained construction, and to read into it conditions and limitations not found there in ordinary English, takes an unfair advantage of the citizens of foreign countries to whom its message is directed.

The suggestion has been made that it is pernicious oversimplification to think that the meaning of a statute is clear simply because its language is plain. But it is believed that statement cannot fairly be made of a statute which applies

only to citizens of foreign countries, who cannot have any way of looking through the plain language of a statute and ascertaining what other and different meaning might possibly be ascribed to it by a court astute in discovering some assumed purpose of Congress. It is submitted that such a statute should be interpreted like a treaty, a truce, a safe conduct or any other document or message of international impact, according to standards of universal meaning and common understanding. (*Cf. Santovincenzo* v. *Egan*, 284 U. S. 30). Its full meaning, intent and purpose should be ascertained only by resort to its language. Otherwise, the document will merely serve as a trap for those to whom it is directed and who have acted on the faith of it, in reliance on the integrity of the United States Government.

In this particular instance, Congress did not say that securities and commodities transactions of a nonresident alien effected here through resident brokers would not constitute doing business here ~~unless~~ only if no one except the resident brokers in any way participated in the transactions, or ~~unless~~ only if the exercise of judgment and discretion which necessarily precedes the effecting of such transactions occurred, and the orders originated, abroad; nor did Congress say that such transactions would not constitute doing business only if they were small in volume. Congress said flatly that the effecting of such transactions by a nonresident alien should not constitute carrying on trade or business in this country, and that, it is submitted, should be interpreted to mean "in any circumstances and under any conditions". (*Cf. Nielsen* v. *Johnson*, 279 U. S. 47).

The enactment in 1936 of the new scheme for taxing nonresident aliens and foreign corporations, embodied in Sections 211 and 231, was a part of this Government's response to a world-wide demand for the elimination of the

evil of international multiple taxation. The international aspect of the problem of taxing the earnings of foreign enterprises not engaged in trade or business in the United States had been recognized in the convention and protocol between the United States and France (of which country the petitioner is a resident) signed April 27, 1932, and effective January 1, 1936, which exempted from tax by one State profits of an enterprise of the other State not allocable to a permanent establishment in the former State. A second convention and protocol with France expressly exempted from the United States tax on capital gains individuals resident in France as well as French enterprises. This second convention and protocol was signed at Paris on July 25, 1939, and was regarded as effective in France on December 22, 1939. However, due to the outbreak of war on September 1, 1939, the United States Senate deferred action on the treaty until after the German armies were driven from France, and gave its advice and consent to ratification on December 6, 1944.

Article 11 of the convention provides:

> "Gains derived in one of the contracting States from the sale or exchange of stocks, securities or commodities by a resident or a corporation or other entity of the other contracting State shall be exempt from taxation in the former State, provided such resident or corporation or other entity has no permanent establishment in the former State."

If this provision had become effective in the United States when it was treated as being in effect in France, petitioner would clearly have come within it as he was a resident of France and admittedly had no permanent establishment in the United States.

Similar clauses are found in Article IX of the convention and protocol between the United States and Sweden signed March 23, 1939, and in Article VIII of the convention and protocol between the United States and Canada signed March 4, 1942.

In Article XIV of the convention and protocol between the United States and the United Kingdom signed June 6, 1946, it is provided:

> "A resident of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States tax on gains from the sale or exchange of capital assets."

This exemption by one country of capital gains realized there by residents of another country, otherwise than through the conduct of a regular business enterprise, simply gave recognition to the principle that the only proper place for the taxation of such gains is the country of domicile. In view of the close relationship between the provisions of Section 211 and the treaties referred to above, the new concept which has been introduced into Section 211 by the courts below, if allowed to go unquestioned, may seriously affect the application of the treaties.

It is important to our relations with foreign countries and to a co-ordination of treaty and statutory provisions that the construction of Section 211 as to engaging or not engaging in business in the United States should not be left strained and indefinite, and that it should be clarified and made certain by this Court.

3. Although technically no conflict exists between Courts of Appeals, the opinion of the Tax Court, on which the Court of Appeals affirmed, assumes a basic premise for its decision contrary to a later decision of the same court,

which the Commissioner chose not to appeal and in which he announced his acquiescence (Int. Rev. Bull. 1948-24-12967). The opinion states that had the petitioner been in the United States during the period of the transactions in 1941 he would have lost the status of nonresident alien, and concludes that the result should be the same because the decisions were made in this country (R. 6, 7). In *Constantinescu* v. *Commissioner,* 11 T. C. 36, it was held that a nonresident alien, who had been physically in this country from 1940 to November, 1945, was not taxable on profits from stock transactions effected through resident brokers on orders given by the nonresident alien while actually here. In that case, notwithstanding that the judgment and discretion were exercised and the orders originated in this country, it was concluded that the nonresident alien was not doing business here under the provisions of Section 211(b). This conclusion accords with the fundamental principle of our tax law that in determining the taxability of sales of personal property, the place where the sales were effected controls, irrespective of where the antecedent discretion was exercised or the orders originated. Thus, in exempting the *effecting* of certain transactions here, Congress exempted the only step in the transactions which could conceivably give rise to tax.

It may be noted that, as a result of complaints that many refugees from abroad who retained the status of nonresidents were able extensively to engage in capital transactions without tax liability, the Revenue Revision Bill of 1948 (H. R. 6712), which passed the House in June 1948, contained in section 143 an amendment to section 211(a), by which the taxability of capital gains of a nonresident alien was made to depend on his physical presence in the United States. (See Report of Committee on Ways and Means, No. 2087, 80th Cong., 2d Sess., May 28, 1948, p. 7.)

The occasion for the amendment, recognized to be necessary to accomplish such taxation, was stated by the Ways and Means Committee as follows (Report No. 2087, 80th Cong., 2d Sess., May 28, 1948, p. 7):

> "Under existing law capital gains of nonresident aliens not engaged in a trade or business in the United States are exempt from income tax. A number of cases have been brought to the attention of your committee in which nonresident aliens are escaping the capital gains tax, although in fact they are in this country for considerable periods and carry out transactions by which gains are realized."

It is accordingly evident that the decision in the *Constantinescu* case is in accord with Congressional understanding of the existing law.

4. Even assuming that the express provision of Section 211(b) were not applicable, the Court of Appeals, in deciding that the petitioner's transactions in commodities constituted carrying on trade or business within the meaning of Section 211(a) of the Internal Revenue Code, decided a question of federal tax law in a way probably in conflict with the decisions of this Court in *Deputy* v. *du Pont,* 308 U. S. 488; *Higgins* v. *Commissioner,* 312 U. S. 212; *City Bank Farmers Trust Company* v. *Helvering,* 313 U. S. 121; and *United States* v. *Pyne,* 313 U. S. 127.

In *Deputy* v. *du Pont,* Mr. Justice Frankfurter said that carrying on trade or business "involves holding one's self out to others as engaged in the selling of goods or services." That remark was apparently adopted by this Court in the other cases cited above, which have generally been understood as holding that the mere purchase and sale of property by a person for his own account, as an investment or speculation, as distinguished from acting as a

broker for others or selling as a dealer or merchant to customers, does not constitute carrying on trade or business within the meaning of the income tax law. It has been suggested that none of the cases cited dealt with extensive speculative operations, but it is to be noted that in *Higgins* v. *Commissioner,* in which this Court affirmed a decision of the Second Circuit, certiorari was granted on the ground of a conflict with the decision of the Sixth Circuit in *Kales* v. *Commissioner,* 101 F. (2d) 35, which did involve extensive speculative operations. Accordingly, it seems clear that this Court did not regard the difference between investment and speculative activities as controlling. The transactions of petitioner in this case being solely for his own account, under the above-cited decisions of this Court it would appear that petitioner should not be regarded as carrying on a trade or business.

Wherefore it is respectfully submitted that the petition should be granted.

March 1, 1949.

Respectfully submitted,

HUGH SATTERLEE
MITCHELL B. CARROLL
ROLLIN BROWNE
Attorneys for Petitioner.